

CIA/OER/S-06645-74 A YEAR LATER: IMPACT OF HIGHER
OIL PRICES ON LATIN AMERICA SECRET

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A Year Later: Impact of Higher Oil Prices on Latin AmericaGeneral

1. High oil bills are now creating serious balance-of-payments problems for the majority of Latin American countries that are significant oil importers. Most of their governments are being forced to curb other imports, slowing economic growth and adding to inflationary pressures. The impact has been the most severe on Brazil, Chile, Paraguay, Uruguay, the six Central American countries, and most of the Caribbean countries.

2. The balance of payments impact on the countries that supply most of their own petroleum requirements -- Argentina, Colombia, and Peru -- has been moderate. At the same time, net oil exporters -- Venezuela, Ecuador, Bolivia, and since June, Mexico -- have benefited substantially from higher prices.

3. During much of 1974, the impact of high oil prices on the foreign payments positions of the oil importing countries was cushioned by booming prices for the region's major export commodities, such as coffee, grains, and minerals. Additionally, several countries were able to obtain loans from the International Monetary Fund (IMF) Oil Facility to help finance the increased oil costs.

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4. Nevertheless, economic activity was hit by the high oil bills. Government reliance on curbing oil consumption through high prices for consumers added to already severe inflation problems. Economic growth rates slipped as governments introduced anti-inflation programs and losses of oil payments from the income stream began to be felt. The situation worsened in the second half of the year as recessions in the industrial countries began to reduce world market prices for the region's exports.

5. During 1975, the depressing effects of higher oil bills and recessions in the industrial countries will lead to a further deterioration in the payments positions of the oil importing countries. Prices of many primary commodity exports are continuing to decline, while prices of imported food and manufactured goods are likely to remain high. Thus, the governments probably will have to further reduce raw materials and capital goods imports needed for economic growth to maintain essential oil supplies. The outlook for 1975 therefore is for a substantial slowing of economic growth and rapidly mounting inflationary pressures in the majority of Latin American countries.

Brazil

6. Brazil's balance of payments deficit is likely to reach \$1.5 billion this year, in contrast to a surplus

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of \$2.2 billion in 1973. The trade deficit will exceed \$6.0 billion this year, up from nearly \$800 million last year. Imports are booming because of higher cost oil and manufacturers efforts to stockpile imported materials in short supply. At the same time, export growth has declined to less than 20% in 1974, compared with 55% last year. Brazil's export performance was limited by a weakening coffee market, a poor cotton crop, restrictions on beef exports, and the sale of most of the soybean crop when prices were at their lowest for the year. Despite large capital inflows, more than \$1.0 billion of the country's foreign reserves will have to be drawn down to finance the current account deficit. Slower export growth and the dampening impact of anti-inflation measures has reduced GNP growth to 9%-10%, down from nearly 12% in 1973.

7. The economic growth rate will slow even more in 1975. Import growth will be curbed severely in order to prevent a further heavy draw down of foreign reserves. While export performance should improve because of the booming sugar market and strong soybean prices, the vital inflow of foreign capital has faltered badly in recent months and its outlook for next year is uncertain. Moreover, interest payments on foreign debt will rise sharply in 1975 absorbing a significant share of the expected increase in export earnings.

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Chile

8. Record copper production and world prices combined with rescheduling of foreign debt payments and a \$60 million loan from the IMF Oil Facility are largely offsetting Chile's sharply higher oil bill this year. The balance-of-payments deficit, although still \$200 million, is the smallest since 1970. Efforts to halt runaway inflation, caused in part by higher oil prices, are hampering economic recovery from the Allende period. The expected 5% 1974 gain in real GNP will only restore output to the 1972 level. Next year, lower copper prices will cause a sharp deterioration in the balance of payments. Export earnings could fall by as much as two-fifths -- if copper prices remain near the present 60 cents per pound -- forcing Santiago to cut back imports and thus further slowing economic growth.

Uruguay

9. Uruguay, among Latin countries, is experiencing the greatest difficulty financing the higher oil import bill, although it has received \$20 million -- equal to nearly 15% the 1974 oil bill -- from the IMF Oil Facility. Beef, the country's major export, has been hit by a Japanese ban on beef imports in February and the European Economic Community (EC) ban in July. Because of Uruguay's poor credit rating and limited foreign reserves, Montevideo is cutting back imports of raw materials and intermediate goods. Economic activity is not growing and

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may even be declining this year. Next year will bring little improvement, particularly if the EC retains its ban on imported beef.

Central America

10. The six Central American countries have experienced increased balance-of-payments problems this year partly because of high oil import bills. Higher prices for the region's main exports, particularly coffee and cotton, offset only part of the oil bills. Despite IMF Oil Facility loans to Costa Rica and El Salvador, all may well incur payments deficits in 1974. Honduras' economic problems have been compounded by hurricane damage to bananas, its leading export. Balance of payments problems probably will become more severe next year because of continuing high prices for imported oil and capital goods, although the problems of Guatemala and Nicaragua could be eased if cotton prices remain high. The slowing of world economic activity may hit Panama's financial industry in 1975, reducing previously large capital inflows and factor receipts.

Caribbean Area

11. The benefits to most Caribbean sugar and bauxite producers from strong export markets are offsetting much of their higher oil bills. The Dominican Republic, for example, is likely to have a trade surplus, largely

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reflecting booming sugar prices. Rising earnings from bauxite and alumina are boosting foreign exchange earnings in Jamaica and Guyana. Economic growth in the Dominican Republic has been strong this year and could remain so in 1975. On the other hand, domestic economic problems are offsetting improved exports in Jamaica and Guyana. Little growth is likely this year or next. Most of the smaller islands are having a difficult time financing higher oil bills. Their sugar and banana export industries are declining or, in some cases, have been abandoned. Moreover, prospects for tourism next year are dim.

Other Countries

12. Countries that are nearly self-sufficient in oil -- Argentina, Colombia, and Peru -- are experiencing little difficulty in financing oil imports. High prices for major exports, especially in the first half of the year have boosted foreign exchange earnings, keeping the oil bill below 12% of projected export earnings. The net oil exporters -- Venezuela, Ecuador, Bolivia, and since June, Mexico -- obviously are gaining substantially from higher foreign exchange earnings. Trinidad and Tobago and the Netherlands Antilles, which process imported crude oil for reexport, are benefiting from higher receipts from oil companies.

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Exploration Activity

13. Greatly increased oil exploration offers promise for the long-term for several countries but little relief in the near term. Exploration is continuing in the promising areas east of the Andes Mountains and in coastal and offshore areas in the Atlantic, Pacific, and Caribbean. Offshore oil has been found along the Central American coasts, and Mexico recently discovered large new fields. If the Mexican government adopts a maximum development policy, 1975 production could reach one million barrels per day. Stepped up exploration and development in Brazil is likely to increase oil output by 35% in 1975 although large imports will still be required.

14. In contrast, government policies in some countries are slowing exploration activity. In Venezuela, proved reserves have been declining because of limited government exploration and Caracas' unwillingness to grant new concessions to private companies. Current low petroleum prices in Colombia hinder increased exploration while oil companies await a new price policy. Additionally, increasingly nationalistic policies in Ecuador have reduced foreign companies' interest in exploring for oil.

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	Gross Foreign Reserves (Million US \$)		Balance of Payments Position (Million US \$)		Net Oil Outlays or Earnings (Million US\$)		Real Rate of Economic Growth (Percent)	
	1973	31 December Most Recent 1973 (Preliminary)	1973 (Estimated)	1974 (Projected)	1973 (Projected)	1974 (Projected)	1973	1974
Argentina	1,318	1,823	642.	100	-185	-525	5.0	6.0 to 7.0
Bolivia	71	168	7	120	53	190	6.0	7.0
Brazil	6,417	5,485	2,200	-1,500	-1,145	-2,800	11.9	9.0 to 10.0
Chile	40	387	-255	-200	-120	-400	-5.0	5.0
Colombia	534	470	130	50	-38	-45	7.5	6.0
Ecuador	241	354	50	220	177	600	12.0	10.0
Paraguay	57	81	22	-10	-5	-25	5.8	2.0 to 4.0
Peru	551	515	195	35	-50	-140	5.3	3.0 to 5.0
Uruguay	232	202	20	-135	-50	-150	0	0 to 2.0
Venezuela	2,420	4,928	543	5,000	5,294	11,000	7.2	N.A.
Mexico	1,356	1,391	122	180	-252	-352	7.6	6.5
Central America	37	37	100	-200	-190	-500	2.6 to 7.6 (range)	N.A.
Caribbean								
Dominican Republic	88	128	-6	-20	-50	-150	7.5	6.5
Guyana	14	13	-24	-50	-22	-80	-3.0	0
Jamaica	128	228	-29	56	-60	-140	0	0 to 2.0

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MEMORANDUM FOR:

Defense Intelligence Agency
Arlington Hall, Room DI-5C4
Phone: 11-25099

The attached report is in response to your 26 November request for information on the impact of higher oil prices on economic performance of Latin American countries. If you need further information, please contact [redacted] our regional analyst, or me on Code 143, Extension 5541.

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Chief, Latin America Branch
Office of Economic Research
Central Intelligence Agency

29 November 1974

(DATE)

FORM NO. 101 REPLACES FORM 10-101
1 AUG 54 WHICH MAY BE USED.

(47)

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MEMORANDUM FOR:

Mr. William Falkner
ARA/ECP, Department of State
Room 3238, Phone: 22385

The attached report is in response to your 15 November request for information on the impact of higher oil prices on the economic performance of Latin American countries. If we can be of further assistance, please contact [redacted] our regional analyst, or me on Code 143, Extension 5541.

25X1A

Chief, Latin America Branch
Office of Economic Research
Central Intelligence Agency

29 November 1974

(DATE)

FORM NO. 101 REPLACES FORM 10-101
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